

A medicine or drug is "any pill, powder, potion, salve, or other preparation intended by the manufacturer for human use and which purports on the label to have medicinal qualities." See 86 Ill. Adm. Code 130.310. (This is a GIL).

September 30, 1999

Dear Mr. Xxxxx:

This letter is in response to your letter dated August 13, 1999. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), enclosed.

In your letter, you have stated and made inquiry as follows:

We would like to have a written opinion regarding the sales taxability of certain items being sold in our grocery and drug stores. The company has recently merged with COMPANY. Even though recent audits have shown we are taxing 98+ percentage of our sales correctly, we cannot assume any future liabilities in the sales tax arena due to small profits eaten up by vague interpretations of the laws. All questionable items will be taxed at the high rate of tax until further instruction is obtained from the Department. We are trying to comply with the laws and protect us from audit deficiencies, while preventing citations from CITY's Department of Consumer Services Weights and Measures, while maintaining customer satisfaction and loyalty through the proper taxing of products. This creates a delicate balancing act! In order to succeed in all areas, we respectfully ask for additional and definitive guidance to the standards, reasoning, and thinking patterns of the Department concerning the areas of concern noted below. Informative answers will deter us from requesting specific rulings on each and every product. Due to our presence in some 38 states, our inventory is very extensive and comprehensive of the entire industry and thus the quantity of products is numerous. We will be happy to assist you in any way we can to accomplish these ends!

We have reviewed many copies of the Medical Appliance Lists (latest copy is dated February 1999) and have reviewed many General Information Letters regarding the law and the interpretations of the law concerning the taxability of the listed products. We are aware of the reduced tax rate on items qualifying for food or medicines. We are also aware of the definition of medicine which states that any pill, powder, potion, salve, or other preparation intended by the manufacturer for human use and which purports on the label to have

medicinal qualities is considered a medicine. Even though this information provides much guidance, questions arise from customers, tax auditors, and us concerning the definition of medicine. Various concerns are noted below.

The first issue involves the retail sales of lip balms. We have spent many hours reviewing product labels and still cannot differentiate between taxable or exempt lip balms. Product labels include many statements such as 'heals cold sores', 'skin protectant', 'advanced protection from the sun', 'restores moisture', 'seals moisture', 'vitamin E enriched', 'contains aloe vera', 'cold sore treatment and prevention', 'removes damaged lip cells', 'treats and heals', 'blister treatment', 'helps healing', 'UVA/UVB protectant', 'flavored skin protectant', 'medicated', and various SPF (Sun Protection Factor) ratings ranging from 7 to 36. Do any of these statements or combination of these statements qualify the product for the reduced rate of tax?

It is simple to determine that a label with the words 'medicated' qualifies for the reduced rate of tax. We have not yet found an explanation as to what qualifies a product's label for usage of the word 'medicated', but we know that these products qualify for the reduced rate of tax. Do you have any guidance concerning this? According to the 1999 edition of Drug Facts and Comparisons used by our pharmacists, sunscreens provide a barrier to sunlight which helps to prevent sunburn, premature aging, photosensitivity reactions, and reduce incidences of skin cancer. A SPF of at least 15 is recommended by the Skin Cancer Foundation. Does a SPF rating affect the medicinal qualities of a product and subsequently allow for the reduced rate of tax? How and where do we draw the line between products taxed at the lower or higher tax rate? Do we need to ask for General Information Letters for all of the different lip balms (approximately 140) inventoried and sold at our stores?

The second issue involves the retail sales of toothpaste. Sunshine support letters 930599 and 930048 indicate that if a label of a toothpaste or tooth polish is marked as medicinal, then it qualifies for the reduced rate. Tooth whiteners do not qualify for the reduced rate. The letters do not mention what qualifies a paste as a medicinal product as interpreted by the Illinois Department of Revenue. None of the products we have reviewed contain the word 'medicated' on the label. Our review does indicate that there are many brands and pastes that prevents cavities, helps to cure bad breath, reduces plaque, helps to prevent gingivitis and gum diseases, and provides whitening characteristics. Most products claim on their label combinations of the above characteristics. A single characteristic toothpaste could not be found. Do these items qualify for the reduced rate of tax? If they do or do not, how do we differentiate the items that should be taxed at the high or low rate?

The third issue is the retail sales of shampoo. Again we understand that if a products label indicates that the product is medicinal, then it qualifies for the reduced rate of tax. Our confusion exists when we have products that are known to be dandruff shampoos. Historically, any dandruff shampoo has been viewed by the auditors as medicated and should be a reduced rate item. Will you please confirm that practice in writing? Are all dandruff shampoos taxed at the reduced rate or is the taxability dependent on the word 'medicated' which must be printed on the label. For example, a manufacture such as Head and Shoulders offers the original formula and advanced formula products for sale. The advanced formula includes the 'medicated' wording on the label. This appears to be a reduced rate item. The original formula advertises the control of dandruff, and the itching and flaking caused by it. Other dandruff manufacturers claim that seborrheic dermatitis, and psoriasis is prevented and controlled. How do you suggest we tax these types of products?

The fourth item is Rogaine. This product contains the drug Minoxidil and should be used under the supervision of a doctor. The label does not appear to say anything concerning medicated but the drug contained therein leads many customers and us astray as to taxability when the Medical Appliance List shows that the high rate of tax is due on this product. Wasn't this product a controlled substance that was regulated by prescription? Isn't Minoxidil a medicine? If so, isn't the medicine contained in the product qualifying it for the reduced rate of tax? Does the potency of the drug within this product cause the taxability to change or is there some other explanation that we can give our customers?

The fifth item is mouthwash. Letter ruling 930048 indicates that not all mouthwashes qualify as medicines. Again, the label determines the taxability of this product. The definition of mouthwash in the Webster dictionary says, 'an antiseptic, usually flavored liquid for cleaning the mouth and freshening breath.' The definition of antiseptic/antiseptis says, 'The destruction of microorganisms that causes disease, fermentation, or putrefaction.' The products that include the verbiage 'medicinal' are clearly medicines but other crafty marketing words confuse customers, frustrate us, and cause questions in auditor's minds. For example, Scope claims that it 'kills bad breath germs'. Plax claims that it 'removes plaque that contains germs and promotes good oral hygiene'. Listerine antiseptic 'kills germs that cause bad breath, plaque, and gum disease, and gingivitis'. Differing opinions have been expressed within the Department concerning these items. How do we tax these items?

The sixth issue concerns soap and antibacterial soap. Letter ruling 950063 indicates that antibacterial soap qualifies for the reduced rate. Does the reduced rate of tax also apply to dish soap and laundry soaps that are incorporating the 'antibacterial' verbiage into their product labeling? The common consumption of soap appears to be

for its cleansing agents and qualities. It has always been promoted as a means of killing germs, cleaning skin and clothes, and maintaining sanitary conditions. Is the antibacterial verbiage a marketing ploy or is there some medicated reasoning that these products are any different than the commonly know uses of soap? How should we tax these products?

The seventh issue involves lotions. The product labels are similar to the lip balm notions noted above. Marketing strategies include verbiage such as 'therapeutic moisturizing', 'heals', 'antioxidants' (prevents premature aging), 'treats eczema, and psoriasis', 'hypo-allergenic', and 'serious medicine for severe dryness'. The Webster dictionary defines lotion as 'a medicated liquid for external application'. Our review discovered a small portion of products containing the word 'medicine' or 'medicated' on the label. How do we tax these products?

Our intentions are to comply with the law while satisfying customers. Uncertain tax rules may damage this balancing act while requiring us as the retailer to be the judge of both sides of the argument. We would appreciate a written document so that we can defend our practices of taxing or exempting these types of products. This would help us also to decipher the taxability of similar type of products in the future.

If you have any additional questions or concerns relating to this please do not hesitate to contact me at ####. Thank you for your help!

In the context of a General Information Letter, we are unable to rule on the taxability of the various products you described in your letter. For your information, we have enclosed a copy of 86 Ill. Adm. Code 130.310, which is the Department's regulation for "Food, Drugs, Medicines and Medical Appliances." This regulation describes how sale of food and drugs can be subject to either low (1%) or high (6.25%) State tax rates under the Retailers' Occupation Tax Act. Local sales taxes may also apply, depending upon where retail sales are made.

A medicine or drug is "any pill, powder, potion, salve, or other preparation intended by the manufacturer for human use and which purports on the label to have medicinal qualities." See Section 130.310(c)(1).

In regards to lip balms, whether a lip balm is taxable depends upon the claim made on the label. If the label indicates that the balm is only to restore moisture or contains aloe vera, the lip balm would be taxable at the high rate of tax. However, to the extent that the label asserts a medicinal quality, such as the healing nature of the product, the lip balm would be subject to the low rate of tax. In order to determine the exact nature of each product, the Department would need to review detailed information in the context of a Private Letter Ruling. We suggest applying the guidelines set forth in this letter and sending

in specific product requests for products that you have difficulty in determining the appropriate tax rate.

Generally, suntan products including sunscreen are subject to the high rate of tax regardless of their SPF rating. As stated above, the same item may be subject to either the low or high rate of tax depending upon whether the company makes a medicinal claim on the brand label. An example is toothpaste. If the label merely says "freshens breath", then the toothpaste would be subject to the 6.25% rate of tax. Alternatively, if the label were to say "kills germs" then the toothpaste would be subject to the low 1% rate of tax.

In regards to shampoo, if the shampoo label makes medicinal claims, then the shampoo is taxable at the low rate. Otherwise, the shampoo is taxable at the high rate. Cosmetic treatments to help grow hair, such as Rogaine, generally would not qualify as medicine or drugs eligible for the low rate.

Regarding the mouthwash, our experience has been that most mouthwashes do not make a medical claim on the label and consequently are subject to the full rate of tax. We do not believe that claims for a product which include "mouth refreshment, fighting strong mouth odors, breath control, freshens your breath, or daily oral care" qualify as medical claims. However, we do consider statements such as "kills mouth germs, or removes plaque bacteria" to be medicinal claims.

Soaps and other chemicals may qualify for the low rate if they are intended by the manufacturer for human use and purport on the label to have medicinal qualities. Soaps that are antibacterial or medicated qualify for the low rate. Lotions also may qualify for the low rate if they meet the above requirements.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of the enclosed copy of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.